

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
HOWARD SCHRIER, MARVIN SCHRIER AND SIDNEY SCHRIER	:	DETERMINATION DTA NO. 806270
for Revision of a Determination or for Refund of Tax on Gains Derived from Certain Real Property Transfers under Article 31-B of the Tax Law.	:	

Petitioners, Howard Schrier, Marvin Schrier and Sidney Schrier, c/o Hartley J. Chazen, Esq., 777 Third Avenue, New York, New York 10017, filed a petition for revision of a determination or for refund of tax on gains derived from certain real property transfers under Article 31-B of the Tax Law.

On January 2, 1991 and January 3, 1991, respectively, petitioners, by Howard M. Koff, Esq. and the Division of Taxation, by William F. Collins, Esq. (Kenneth J. Schultz, Esq., of counsel), waived a hearing and agreed to submit the case for determination based on documentation and memoranda of law to be submitted by March 28, 1991. After due consideration of the record, Robert F. Mulligan, Administrative Law Judge, hereby renders the following determination.

ISSUE

Whether petitioners' original purchase price, for real property transfer gains tax purposes, should be the fair market value of the real property on the date it was transferred to petitioners in a liquidating dividend, or rather the liquidating corporation's carry-over original purchase price of the property.

FINDINGS OF FACT

In 1986, petitioners, Howard Schrier, Marvin Schrier and Sidney Schrier, each owned one-third of the outstanding stock of H. Schrier & Co., Inc. ("the corporation"). The

corporation operated a wholesale food distribution business from its warehouse at 363 Bond Street, Brooklyn, New York.

During 1986, after negotiations extending over a period of more than one year, the corporation sold its operating business assets and good will to a former competitor, Irving Liebertoff, Inc., of Brooklyn, New York. As part of the agreement, petitioners agreed to provide full-time services to the purchaser. The purchaser, however, already owned an under-utilized warehouse and had no use for the corporation's land and building at 363 Bond Street. Consequently, the corporation retained title to the real property.

Petitioners were advised by counsel that, for Federal tax purposes, the corporation had to be liquidated and its real property distributed to petitioners by the end of December 1986.

It was petitioners' intention that they were to act unanimously in disposing of the property. Petitioners were advised by counsel that, in order to provide for unanimity of action, they would have to take title either as joint tenants with rights of survivorship, or under a partnership agreement. Petitioners elected to take title as joint tenants, as they were advised that the drafting of a partnership agreement would be expensive and also that such an agreement could raise Federal income tax problems.

Accordingly, the corporation distributed the land and warehouse building at 363 Bond Street to petitioners, as joint tenants with rights of survivorship, solely in exchange for petitioners' shares of stock in the corporation.

The distribution was accomplished by deed dated December 27, 1986, between SMH Liquidating Corp., formerly known as H. Schrier & Co., Inc., as grantor, and petitioners, as grantees. Petitioners took title as joint tenants with rights of survivorship. The deed was not recorded until December 18, 1987.

The transaction constituted a liquidation which was taxable for Federal income tax

purposes.

The fair market value of the property on the date of the transfer was \$975,000.00.

The sum of \$325,000.00 (representing one-third of the total fair market value) was used as the selling price in the computation of the long term capital gain on the sale of the corporation's stock, as reported on each petitioner's 1986 Federal income tax return.

The transfer from the corporation to petitioners was exempt from real property gains tax and no tax was assessed or paid with respect to said transfer.

At the time of the liquidation, the corporation's basis for the property was \$212,413.00.

The following New York State real property transfer gains tax questionnaires were filed with respect to the transaction:

(a) Transferor questionnaire. A transferor questionnaire dated December 27, 1986 was executed by H. Schrier & Co., Inc. showing gross consideration paid of \$975,000.00, said sum representing the fair market value of the land and building at the date of the transfer to petitioners upon dissolution of the corporation. The purchase price paid to acquire the property was stated to be \$226,735.00, with capital improvements of \$238,625.00, for a total original purchase price of \$465,360.00. The gain subject to tax was stated as zero.

(b) Transferee questionnaire. A transferee questionnaire also dated December 27, 1986 was executed by petitioners showing consideration of \$975,000.00, again representing the fair market value of the land and building at the date of transfer upon dissolution.

It appears that petitioners contracted to sell the premises to Cosmos Forms Ltd., pursuant to a contract of sale dated November 16, 1987, and further, that on November 23, 1987, Cosmos Forms Ltd. assigned its rights under the contract to Fali Realty Corp.

The following New York State real property gains tax questionnaires were filed with respect to petitioners' sale of the property:

(a) Transferor questionnaire. Petitioners executed a transferor questionnaire showing a transfer to Fali Realty Corp., as transferee. The questionnaire, dated November 16, 1987, showed an anticipated transfer date of December 30, 1987. Gross consideration was reported to

be \$1,300,000.00 and the purchase price paid to acquire the property was stated as \$975,000.00. The sum of \$10,000.00 was shown as an allowable selling expense, resulting in a total original purchase price of \$985,000.00. The gain subject to tax was shown as \$315,000.00, with anticipated tax due of \$31,500.00.

(b) Transferee questionnaire. A transferee questionnaire, also dated November 16, 1987, was submitted showing Cosmos Forms, Ltd., as transferee and petitioners, as transferor. The anticipated date of transaction was shown as December 30, 1987 and the consideration was stated to be \$1,300,000.00.

(c) Transferee questionnaire. A transferee questionnaire dated November 23, 1987 was submitted showing the transferee as Fali Realty Corp. and the transferor as Cosmos Forms, Ltd. The consideration paid was shown as zero.

Petitioners paid \$101,758.70 in New York State real property transfer gains tax on or about February 12, 1988.

On or about September 8, 1988, petitioners filed a claim for refund of \$70,258.70, asserting that proper tax due was only \$31,300.00,¹ as their purchase price paid to acquire the property should be \$975,000.00, rather than the corporation's original purchase price of \$465,360.00.

SUMMARY OF THE PARTIES' POSITIONS

Petitioners contend:

- (a) that, since they took title to the subject premises as joint tenants with rights of survivorship, rather than as tenants in common, the carry-over basis rule set forth in 20 NYCRR 590.50(a)(3) is not applicable; and
- (b) that, assuming the liquidating dividend to petitioners is found to constitute a "mere change", the carry-over basis rule of 20 NYCRR 590.50(a)(3) is invalid.

The Division of Taxation claims that no change of beneficial ownership was accomplished

¹As found in Finding of Fact "14(a)", the transferor questionnaire for the transaction indicates anticipated tax due of \$31,500.00.

by the liquidation and thus, it was a "mere change" within the meaning of the statute and regulations. It argues that

the fact that petitioners took title as joint tenants, rather than as tenants in common, should not require the conclusion that a "mere change" did not occur.

CONCLUSIONS OF LAW

A. Tax Law § 1441 imposes a 10% tax on gains derived from the transfer of real property within the State of New York.

B. The term "gain" is defined in Tax Law § 1440.3 as follows:

"'Gain' means the difference between the consideration for the transfer of real property and the original purchase price of such property, where the consideration exceeds the original purchase price."

C. Tax Law § 1440.5 provides, in pertinent part, as follows:

"(a) 'Original purchase price' means the consideration paid or required to be paid by the transferor; (i) to acquire the interest in real property, and (ii) for any capital improvements made or required to be made to such real property, including solely those costs which are customary, reasonable, and necessary, as determined under rules and regulations prescribed by the tax commission, incurred for the construction of such improvements. Original purchase price shall also include the amounts paid by the transferor for any customary, reasonable and necessary legal, engineering and architectural fees incurred to sell the property and those customary, reasonable and necessary expenses incurred to create ownership interests in property in cooperative or condominium form, as such fees and expenses are determined under rules and regulations prescribed by the tax commission.

(b) In the case of a transfer of real property by a gift, devise, bequest or inheritance, the original purchase price of the real property in the hands of the transferee immediately after the transfer shall be the same as the original purchase price of such property in the hands of the transferor immediately before the transfer.

(c) The transferee of every transfer of real property for which exemption is granted, pursuant to subdivision one of section fourteen hundred forty-three of this article on the basis that no consideration was paid for such transfer, shall be bound by a determination of original purchase price as determined under paragraph (b) of this subdivision, if such transferee participated in filing the forms upon which such exemption was granted."

D. Tax Law § 1443 provides, in pertinent part, that a total or partial exemption shall be allowed in the following cases:

"1. If the consideration is less than one million dollars;

* * *

4. Where the transfer of real property is to a corporation upon its organization solely in exchange for the stock or securities in such corporation if immediately after such transfer the person or persons making such transfer are in control. The term control means the ownership of stock possessing at least eighty percent of the total combined voting power of all classes of stock entitled to vote and at least eighty percent of the total number of shares of all other classes of stock of the corporation.

5. If a transfer of real property, however effected, consists of a mere change of identity or form of ownership or organization, where there is no change in beneficial interest."

E. Regulations at 20 NYCRR 590.50 interpreting the "mere change of identity" provision of Tax Law § 1443.5 provide, in pertinent part, as follows:

"(a) Question: Section 1443(5) of the Tax Law exempts a transfer from the gains tax to the extent it 'consists of a mere change of identity or form of ownership or organization, where there is no change in beneficial interest.' Does this exempt:

* * *

(3) The transfer of real property by a corporation to its shareholders, who will hold the real property as tenants-in-common in the same pro rata share as they own the corporation?

Answer: Yes. This is a mere change of identity or form of ownership or organization. The shareholders will have a carry-over original purchase price in the real property.

* * *

(b) Question: When the exemption applies, how is the carry-over original purchase price of the real property as held under the new form of ownership calculated?

Answer: The mere change exemption requires a carry-over original purchase price to the extent the mere change exemption applied.

Example: B owns real property with a fair market value of \$10 million. B's original purchase price is \$6 million. B transfers the property to a partnership in exchange for a 30-percent interest in the partnership assets. Although B has transferred all of the real property to a partnership, he is entitled to a mere change exemption from tax of 30 percent.

\$10,000,000	consideration
- 6,000,000	original purchase price
\$ 4,000,000	total gain
x 30%	
\$ 1,200,000	exempt gain
2,800,000	taxable gain

The partnership then has an original purchase price in the property of \$8,800,000 (\$6,000,000 + \$2,800,000, B's original purchase price plus B's taxable gain.)

(c) Question: How does the mere change of identity exemption interrelate with the million-dollar exemption?

Answer: The million-dollar exemption is applied to consideration first and then the mere change exemption is applied. A transfer in which the consideration is greater than \$1 million will remain taxable, the mere change exemption only defers payment of tax on the portion of gain determined to be attributed to a mere change in form of ownership."

Regulations at 20 NYCRR 590.53, with respect to dividends of real property, provide as follows:

"(a) Question: Is a dividend declared by the board of directors in the form of unencumbered real property (other than a liquidating distribution), where the shareholders will individually hold title to separate parcels of real property of equal value, subject to the gains tax?

Answer: Yes. However, since the payment of such a dividend is not supported by any consideration, there is no taxable gain. On a subsequent transfer of the real property received as a dividend, the original purchase price of such real property will be the pro rata share of the original purchase price of the corporation attributable to such property.

Question:² If such a dividend was a liquidating dividend, would the result be different?

Answer: Yes. In the case of a liquidating dividend, the transfer is for the consideration of the interest in the entity given up, such consideration being equal to the fair market value

of the real property. (See section 590.50 of this Part for the application of the mere change exemption.)"

F. Petitioners have attempted to distinguish this case from the example in 20 NYCRR 590.50(a)(3) on the basis that the deed running from the corporation to petitioners conveyed

title to them as joint tenants with rights of survivorship, rather than as tenants in common. This distinction, however, is immaterial for gains tax purposes. The aforesaid example is nothing more than one illustration of what is meant by "mere change of identity". While joint tenancies are distinguishable from tenancies in common (EPTL 6-2.2), and result in a deceased joint tenant's interest running to his surviving joint tenants, rather than his estate or heirs, it is noted that a joint tenant may maintain an action for partition (or sale) under RPAPL 901.1. A partition of property held by joint tenants terminates the joint tenancy (24 NY Jur 2d, Cotenancy and Partition, § 33). Accordingly, at any time after delivery of the deed, any or all of the petitioners could have extinguished the joint tenancy and could have obtained one-third of the real property or one-third of the proceeds of the sale thereof. In view of this, there is no reason why joint tenancies should be treated differently from tenancies in common under Article 31-B of the Tax Law.

G. Next to be examined is petitioners' argument that the carry-over original purchase price rule of 20 NYCRR 590.50(a)(3) is invalid. Petitioners note that the carry-over purchase price is specifically provided for by statute in cases of transfers by gift, devise, bequest or inheritance, but not in cases involving a "mere change" exemption. Consequently, petitioners argue, the statute can not be expanded by regulation to apply the carry-over purchase price in situations where there is a mere change of identity or form of ownership or organization.

Tax Law § 1440.5(b), as petitioners point out, provides for a carry-over original purchase price in the event of inter vivos or testamentary gifts. Also, Tax Law § 1440.5(c) establishes a rule by which a transferee who participates in filing forms stating that a transfer was exempt on the basis that no consideration was paid, is bound by the transferor's basis. It is noted that said provisions are applicable only in cases of transfers which are not supported by consideration. The transfer from the corporation to petitioners, on the other hand, was not a gift, but constituted a transfer for a consideration and, as such, is to be considered independently of Tax

Law § 1440.5(b) and (c).

While the statute does not specifically provide for a carry-over original purchase price in cases of "mere change", ³ the regulation does so provide, and thus establishes a rational and practical method for determining the original purchase price in cases where there has been a transfer for a consideration which was exempt as a "mere change". Said regulation is not disharmonious with Tax Law § 1440.5(b) nor any other statutory provision and is therefore valid.

H. The distribution of the property to petitioners clearly constituted a "mere change of identity" within the meaning of Tax Law § 1443.5. Accordingly, petitioners' original purchase price is the corporation's carry-over original purchase price.

I. The petition of Howard Schrier, Marvin Schrier and Sidney Schrier is denied, and the denial of petitioners' claim for refund is sustained in full.

DATED: Troy, New York

ADMINISTRATIVE LAW JUDGE

³It is noted that the statute is also silent as to carry-over original purchase price where real property is transferred to a corporation in exchange for stock. Such transfers, which clearly are for a consideration, are also exempt (Tax Law § 1443.4).